

Message Text

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(EDRC): REVIEW OF DENMARK, MARCH 9, 1978

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1. SUMMARY: DANISH DELEGATION (HEADED BY LOHSE OF
MINISTRY ECONOMIC AFFAIRS INCLUDING REPS FROM FINANCE,
LABOR AND THE NATIONAL BANK) CAME PREPARED TO EXPURGATE
ANY REFERENCE TO KRONER DEVALUATION FROM THE 1978 SURVEY
OF DENMARK AND TO PRESAGE A NEW COMPREHENSIVE MEDIUM-
TERM INCOMES POLICY TO BE UNVEILED THIS SUMMER. THIS
POLICY PACKAGE WILL BE DESIGNED TO MOBILIZE ALL INSTRU-
MENTS OF GOVERNMENT POLICY TO RESTORE DENMARK'S INTER-
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NATIONAL COMPETITIVE POSITION BY REDUCING DOMESTIC COSTS,
RAISING PROFITABILITY AND INVESTMENT, THEREBY LEADING
TO HIGH EMPLOYMENT. DETAILS WERE NOT GIVEN, BUT LOHSE
SIGNALLED CLEARLY THAT THE OVERHANG OF CURRENT POLICY,
PARTICULARLY WAGE INDEXATION PORTIONS NOW FUNDED BY THE
GOVERNMENT, WOULD BE HANDLED SO AS TO LIFT THE COSTS
PERMANENTLY FROM THE SHOULDERS OF EMPLOYERS, AT LEAST

DIRECTLY. DISCUSSION OF SECRETARIAT'S LABOR MARKET AND WAGE DIFFERENTIAL STUDY RESULTED IN AGREEMENT TO DISAGREE ON SEVERAL POINTS, WHILE THE TEXT OF THE SURVEY WILL BE MODIFIED SLIGHTLY TO AVOID SUGGESTING THAT NARROWING OF WAGE STRUCTURES HAS GENERATED "PENT-UP" PRESSURES. DANISH DELEGATION AND SECRETARIAT GENERALLY AGREED ON 1978 FORECAST, WHILE FOR 1977 EDRC FELT THAT SECRETARIAT'S TONE WAS A BIT TOO NEGATIVE AND DECIDED TO PLACE MORE BLAME ON GLOBAL CONDITIONS AND MOTHER NATURE. CLEAR AND CONSTRUCTIVE INPUT FROM EMBASSY COPENHAGEN AND WASHINGTON AGENCIES MUCH APPRECIATED. END SUMMARY

2. RECENT TRENDS AND 1978 FORECAST: DANISH DELEGATION WAS IN GENERAL AGREEMENT WITH SECRETARIAT'S DESCRIPTION OF 1977 PERFORMANCE AND OUTLOOK FOR 1978. COMMITTEE AND DANISH DELEGATION FELT, HOWEVER, THAT REPORT DID NOT SUFFICIENTLY RECOGNIZE POSITIVE ELEMENTS OF DANISH PERFORMANCE, PARTICULARLY THOSE POLICY-INDUCED, NOR EXTENT OF NEGATIVE IMPACT OF TEMPORARY FACTORS (E.G., 76/77 CROP) AND SLOW WORLD TRADE GROWTH. RELEVANT PASSAGES OF SURVEY WILL BE REVISED TO PUT DANISH POLICY IN MORE POSITIVE LIGHT. SOME MARGINAL DIFFERENCES OF OPINION ON UNEMPLOYMENT RATE (DANES FELT 9-1/2 TOO HIGH FOR END 1978 SINCE IT IS 1ST QUARTER 1978 NOT SEASONALLY ADJUSTED), BOP PROFILE (IMPROVING IN FIRST HALF 1978, WITH SLOWER IMPROVEMENT IN SECOND VS. DETERIORATION PER SECRETARIAT), LIMITED OFFICIAL USE

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AND INFLATION (DANES FEEL 1977 EVIDENT ACCELERATION WAS DUE TO TAX AND EXCHANGE RATE FACTOR SO THAT UNDERLYING RATE DECELERATING) DID NOT DETRACT FROM AGREED APPRECIATION OF PRESENT SITUATION.

3. ECONOMIC POLICY: DANISH DELEGATION PLACED ECONOMIC POLICY DECISIONS SQUARELY IN CONTEXT OF BALANCE-OF-PAYMENTS CONSTRAINT AND PERCEIVED NEED TO IMPROVE DANISH COMPETITIVE POSITION. GIVEN OPENNESS OF ECONOMY, HIGH IMPORT PROPENSITY, LARGE OUTSTANDING DEBT, RECENT HIGH DOMESTIC PRICE AND COST INFLATION, DANISH AUTHORITIES RECOGNIZE THAT BALANCE-OF-PAYMENTS DEFICIT MUST BE BROUGHT BACK TO MANAGEABLE LEVEL. (NEVERTHELESS, DENMARK FEELS THAT IT COULD PARTICIPATE TO A SMALL EXTENT IN A CONCERTED ACTION ("CONVOY") PROGRAM IF MANEUVERING ROOM WERE PROVIDED BY EXPANSION IN MAJOR TRADING PARTNERS). ON POLICY ACTIONS NEEDED TO RESTORE COMPETITIVENESS, DANISH DELEGA-

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TION FLATLY, AND WITH SOME IRRITATION, REJECTED SECRETARIAT'S VEILED SUGGESTIONS THAT KRONER BE SUBSTANTIALLY DEVALUED. (FYI -- IT SEEMS THAT CAREFUL READING OF PARAGRAPH 74 OF DRAFT SURVEY REVEALS THIS SUGGESTION. END FYI) LOHSE SAID DEVALUATION WOULD ONLY HAVE CIRCULAR PRICE EFFECTS, WOULD NOT OF ITSELF IMPROVE COMPETITIVE POSITION, BUT RATHER WOULD DESTROY ANY HOPE OF A MEANINGFUL AND COMPREHENSIVE INCOMES POLICY. HE WAS MORE FLEXIBLE ON POSSIBILITY THAT KRONER BE marginally "ADJUSTED" (BUT NOT ON A REGULAR BASIS) TO PREVENT UNDUE INFLUENCE FROM BEHAVIOR OF A SINGLE CURRENCY (READ DM), BUT NEVERTHELESS DESCRIBED "SNAKE" AS "NICE FIXING POINT."

4. LOHSE TOLD COMMITTEE THAT DANISH GOVERNMENT APPROACH TO MEDIUM-TERM PROBLEMS, PARTICULARLY COMPETITIVENESS, WOULD BE MAJOR NEW INCOMES POLICY INITIATIVE TO BE REVEALED THIS SUMMER, WITH EFFECT TO 1981 OR POSSIBLY 1983. THIS POLICY WOULD SEEK TO RESTORE DANISH INTERNATIONAL COMPETITIVE POSITION THROUGH SLOW REAL GROWTH

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OF HOUSEHOLD INCOMES (REAL WAGE VIRTUALLY FLAT), WHILE CREATING CONDITIONS CONDUCIVE TO PRIVATE INVESTMENT,

THUS RESTORING PRODUCTIVITY GROWTH, AND LOWERING UNIT COSTS. PACKAGE WOULD INCLUDE WIDE RANGE OF POLICY MEASURES INCLUDING TAXES, HOUSING INCENTIVES, TREATMENT OF BLOCKED FUNDS, ETC. TO SPREAD THE IMPACT AS WIDELY AS POSSIBLE THROUGHOUT THE ECONOMY. CURRENT FISCAL AND INCOMES POLICY ARRANGEMENTS SUCH AS SUPPLEMENTARY PENSION FUND (SPF) AND OTHER LABOR COSTS WHICH WOULD FALL ON EMPLOYERS AT END 1978 (THE SO-CALLED "ATOMIC BOMB") WOULD BE HANDLED SO AS TO MINIMIZE IMPACT ON COSTS. IN THIS REGARD, GOVERNMENT HOPES CONSENSUS WILL DEVELOP ON INTRODUCTION OF SOME FORM OF "ECONOMIC DEMOCRACY" TO GIVE WORKERS CLAIM TO PROFITS IN LIEU OF INDEXATION SCHEME, THUS NEUTRALIZING POTENTIAL COST AND DEMAND EFFECTS OF ACCUMULATED SPF FINANCIAL ASSETS AND INDEXATION PORTIONS "IN PERPETUITY." LOHSE WAS UNABLE TO GIVE DETAILS OF GOVERNMENT'S PROPOSAL -- BUT SAID IT WOULD BE COMPREHENSIVE AND WOULD EVENTUALLY EMBODY A CONSENSUS OF THE ECONOMIC PARTNERS, PARTICULARLY WHEN VIEWED "IN THE LIGHT OF POSSIBLE ALTERNATIVES," NAMELY STILL HIGHER UNEMPLOYMENT.

5. ON OTHER POLICY SPECIFICS, LOHSE OPINED THAT THE LARGE GOVERNMENT DEFICIT PRESENTED NEITHER A POLITICAL NOR FINANCING PROBLEM. ON THE LATTER, THE GOVERNMENT USES THE VOLUME OF BONDS ISSUED AS A POLICY INSTRUMENT TO REGULATE MONETARY CONDITIONS -- IF, THEREFORE, FINANCING THE GOVERNMENT DEFICIT FROM HOUSEHOLD SAVINGS THREATENS TO CROWD OUT BUSINESS INVESTMENT, GOVERNMENT WOULD GO ELSEWHERE; E.G., ABROAD OR TO THE CENTRAL BANK. NEITHER IS CREDITWORTHINESS A PROBLEM -- AS LONG AS THE CURRENT ACCOUNT DEFICIT WAS MOVING IN THE RIGHT DIRECTION. LIMITED OFFICIAL USE

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TION (GETTING SMALLER) WHICH IS NOW THE CASE, ACCORDING TO LOHSE. IN RESPONSE TO A QUESTION, LOHSE GAVE THE DEBT SERVICE, ON BASIS OF CURRENT OUTSTANDING OFFICIAL DEBT, AS KR. 5 BILLION IN 1978, KR. 6 BILLION - 1979, KR. 6.5 BILLION - 1980 AND LEVELLING OUT. WITH RESPECT TO INDUSTRIAL POLICY, LOHSE NOTED THAT DENMARK HAD, WITH FEW EXCEPTIONS, REJECTED TEMPORARY EMPLOYMENT SUPPORTING SCHEMES AND INDUSTRIAL/SECTORAL SUBSIDIES, CITING THAT DENMARK FOLLOWED A LIBERAL POLICY BY WHICH A "FIRM MUST DIE IF IT CANNOT COMPETE." SHIPYARDS WERE CITED AS AN EXCEPTION SINCE "EVERYONE ELSE WAS DOING IT, SO DENMARK HAD TO GO ALONG."

6. LABOR MARKET AND WAGE DIFFERENTIALS: DANISH DELEGATION AND COMMITTEE COMPLIMENTED SECRETARIAT'S ANALYSIS OF THIS SUBJECT. LOHSE CONTENDED, HOWEVER, THAT MOST DANISH UNEMPLOYMENT WAS "CYCLICAL" (VS. LAREMAJORITY

NON-CYCLICAL ACCORDING TO SECRETARIAT) BUT WHEN PUSHED BY SPECIFIC QUESTIONS AGREED THAT LARGE PORTION REQUIRED MEDIUM-TERM SOLUTIONS DUE TO RECENT ACCELERATION OF LABOR SUPPLY, CURRENT CAPITAL SHORTAGE, CURRENT BOP CONSTRAINT, AMONG OTHERS, AND THAT FRICTIONAL ELEMENT WAS LARGER THAN IN PAST. LOHSE SUGGESTED, HOWEVER, THAT INTERNATIONAL UNEMPLOYMENT STATISTICS WERE SO INFLUENCED BY GOVERNMENT LABOR MARKET POLICY THAT THEY WERE NOT NECESSARILY A RELIABLE GAUGE FOR OTHER POLICY DECISIONS, NOR INTERNATIONAL ANALYSIS OF ECONOMIC SITUATION. HE CONTRASTED SWEDISH AND DANISH POLICY IN THIS RESPECT, NOTING THAT DENMARK

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HAD VIRTUALLY NO "HIDDEN" UNEMPLOYMENT, WHEREAS IN SWEDEN SOME 4 PERCENT OF THE LABOR FORCE IS "EMPLOYED" IN SPECIAL EMPLOYMENT SUPPORTING PROGRAMS FINANCED BY THE GOVERNMENT. THE SECRETARIAT'S FINDING THAT WAGE DIFFERENTIALS, BOTH SECTORAL AND OCCUPATIONAL, HAD NARROWED IN DENMARK, WAS NOT SURPRISING, ACCORDING TO LOHSE, SINCE THIS HAS BEEN THE STATED OBJECTIVE OF GOVERNMENT POLICY FOR SOME TIME. HE ADDED THAT THE NARROWED WAGE STRUCTURE HAD COME TO STAY, SINCE IT REFLECTED A CONSENSUS AMONG LABOR MARKET PARTICIPANTS, AND WOULD NOT THEREFORE BE A SOURCE OF FUTURE INFLATIONARY PRESSURES

NOR MAJOR SECTORAL DIFFICULTIES (NOTING THAT THE TEXTILE INDUSTRY HAD READILY ADJUSTED TO THE EQUAL PAY FOR WOMEN RULE OF 1973). THE COMMITTEE WAS GENERALLY SKEPTICAL.

7. CONCLUSIONS: DANISH DELEGATION, SECRETARIAT, AND EDRC HAD A FREE-WHEELING DISCUSSION OF DANISH ECONOMIC SITUATION AND POLICY, BUT NUMEROUS DIFFERENCES OF VIEW LIMITED OFFICIAL USE

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REMAINED, PARTICULARLY WITH REGARD TO THE ABILITY OF THE PROPOSED INCOMES POLICY ALONE TO ADDRESS AND SOLVE THE FUNDAMENTAL PROBLEMS IN THE DANISH ECONOMY -- I.E., REDUCE THE CURRENT ACCOUNT DEFICIT BY RESTORING DANISH COMPETITIVENESS WHILE BOOSTING DOMESTIC ACTIVITY TO A LEVEL CONSISTENT WITH RESTORING HIGH EMPLOYMENT. THE EDRC CHAIRMAN DREW THE FOLLOWING PRINCIPAL CONCLUSIONS FROM THE EXAMINATION:

-- THE EDRC UNDERSTANDS THE DANISH APPROACH TO RESTORING ITS INTERNATIONAL COMPETITIVE POSITION, BUT CONSIDERABLE DOUBT REMAINS THAT CURRENT POLICY IS SUFFICIENT TO REACH DESIRED BOP OBJECTIVES, WHICH ARE CRUCIAL TO RESTORING HIGH EMPLOYMENT. IN PARTICULAR, THE EFFECT OF CURRENT POLICY ON PROFIT LEVELS AND INVESTMENT ARE QUESTIONED.

-- NEVERTHELESS, THE EDRC ACCEPTS POLICY CONCLUSION FOR THE 1978 SURVEY STRESSING THE NEED FOR A STRONG COMPREHENSIVE INCOMES POLICY WITH MEDIUM-TERM OBJECTIVES OF MODERATING NOMINAL LABOR COSTS, RAISING PROFITABILITY (IN PART THROUGH REVIVING INTERNATIONAL MARKETS), AND PROMOTING EMPLOYMENT.

-- NO REFERENCE, HOWEVER, WELL HIDDEN, TO DEVALUATION WILL APPEAR IN THE SURVEY, HOWEVER, SOME MEMBERS OF EDRC, PARTICULARLY THE SECRETARIAT, FEEL THAT EXCHANGE RATE ADJUSTMENT MAY BE NECESSARY. IN THE "SNAKE" CONTEXT, ON THE OTHER HAND, KRONER APPRECIATION IS LIKELY UNLESS POLICY ACTION IS TAKEN TO COUNTERACT IT.
SALZMAN

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